

RECEIVED
FEC MAIL
OPERATIONS CENTER
BEFORE THE FEDERAL ELECTION COMMISSION

2005 SEP 30 P 4:41

Americans for a
Republican Majority,
Corwin Teltschik, Treasurer

)
)
)
)

MUR 5675

**RESPONSE OF AMERICANS FOR A REPUBLICAN MAJORITY
TO THE COMPLAINT FILED BY THE CITIZENS FOR
RESPONSIBILITY AND ETHICS IN WASHINGTON**

By and through the undersigned counsel, Americans for a Republican Majority ("ARMPAC") hereby responds to the complaint filed by the Citizens for Responsibility and Ethics in Washington ("CREW").

CREW's complaint is nothing more than a regurgitation of the recently-completed Report of the Audit Division on ARMPAC ("Final Audit Report"), and adds nothing to the conclusions of the auditors. The Audit Division found no substantive violations of the Federal Election Campaign Act of 1971 (as amended) ("the Act"), but did raise some reporting issues. ARMPAC has already addressed all issues raised by the auditors, and has already amended its reports per the recommendations suggested in the interim audit report. Thus, in light of ARMPAC's full cooperation and its prompt filing of recommended amendments, this is not the sort of matter that requires the additional expenditure of Commission resources. Therefore, ARMPAC respectfully requests that the Commission take no further action.

RECEIVED
FEDERAL ELECTION
COMMISSION
OFFICE OF GENERAL
COUNSEL
2005 SEP 33 P 11:20
RECEIVED
FEDERAL ELECTION
COMMISSION
OFFICE OF GENERAL
COUNSEL
2005 OCT -3 P 1:16

26044142660

I. BACKGROUND

Americans for a Republican Majority ("ARMPAC") is a non-connected committee. First registered on April 22, 1994, ARMPAC qualified for multicandidate status on October 20, 1994. It is headquartered in Washington, D.C.

ARMPAC has been one of the most high-profile "Leadership PACs," due primarily to the notoriety of its Chairman, Congressman Tom DeLay. Having served as both House Majority Whip and House Majority Leader, Mr. DeLay has become a target for many who oppose his conservative politics. He has been the subject of scathing press accounts, Democrat attacks, frivolous FEC complaints, and even accused of racketeering by the Democratic Congressional Campaign Committee, who in 1999 filed suit against DeLay through their lawyers at Perkins Coie. As reported by *The Hill* on March 10, 2004, "House Democratic leaders are honing an election strategy to taint the entire Republican caucus by demonizing Majority Leader Tom DeLay (R-TX)."

Citizens for Responsibility and Ethics in Washington ("CREW") is the latest in a long line of political gadflies attempting to cash in on the latest DeLay craze, furthering the election strategy of House Democrats by demonizing Mr. DeLay. It is run by a former staffer for left-wing Democrats John Conyers, Charles Schumer and Joe Biden.

Picking up where Judicial Watch left off, CREW never misses a chance to issue a self-serving press release or file a frivolous complaint designed to generate headlines at the expense of elected officials. Even a casual review of its website demonstrates this pattern; CREW has filed some version of a complaint against Senate Majority Leader Bill Frist, the Department of Agriculture, the Social Security Administration, Attorney General Alberto Gonzalez, Bush-Cheney '04, the Department of Justice, habitual

Republican candidate Alan Keyes, and even the Federal Election Commission itself. Conspicuously lacking from CREW's self-promoting are attacks against Democrat politicians.

The current complaint¹ is an example of this, and ought to be treated accordingly. It does nothing but regurgitate the final report already issued by the Audit Division. It does not allege any substantive violations of the law, but only raises various reporting issues. Ultimately, ARMPAC cooperated fully with the auditors, and has already filed all amendments suggested by the Audit Division. No further Commission action is warranted.

II. SUMMARY OF AUDIT

The Commission's Audit Division conducted a full audit of ARMPAC, covering the time period January 1, 2001 through December 31, 2002. Oddly, at the threshold of the audit, ARMPAC representatives were informed that the auditors had information that indicated that ARMPAC may have received prohibited funds. The source of this information was not disclosed. The audit disclosed no such violations, and at the conclusion of the audit, the auditors confirmed that there were no prohibited funds. Even more bizarre is that the existence of the audit, specifically the existence of the interim audit report, was confirmed to the *Washington Post* by a "government official" – in other words, someone within the Commission leaked the fact that Tom DeLay's Leadership PAC was being audited.²

¹ In fact, CREW could barely contain itself in anticipation of the release of the final audit report. Prior to its release, CREW claimed it was going to file a Freedom of Information Act suit against the Commission seeking the release of the interim audit report.

² Although ARMPAC believes that the Commission is aware of the confirmation to the *Post*, it does not appear that any sort of formal internal investigation has been undertaken. Thus, ARMPAC requests that an internal investigation be conducted to ascertain the source of the press leak.

Even in the face of evidence of bias and violations, ARMPAC nonetheless cooperated fully with the audit. In fact, the auditors did not find any substantive violations of the Act or Commission regulations. On the contrary, the auditors found that ARMPAC "satisfied the minimum recordkeeping requirements of 11 CFR 102.9." Final Audit Report at 1. The only issues raised by the auditors concerned reporting. ARMPAC followed all of the recommendations of the auditors, and accordingly has already filed amended reports.

III. ANALYSIS

The auditors made findings in three areas: (1) misstatement of financial activity; (2) reporting of debts and obligations; and (3) non-federal funding of federal activity.

A. *Misstatement of Financial Activity*

The Audit Division's first finding (and as regurgitated by the complainant) concerned misstatement of financial activity. Not an uncommon finding, the Commission has routinely not pursued such issues in enforcement, absent aggravating factors not present in the ARMPAC audit.³ As the auditors made clear, "[i]n response to the interim audit report, ARMPAC filed amended reports that materially corrected the misstatements." Final Audit Report at 1, 6. The Commission has on occasion dealt with such issues through its Alternative Dispute Resolution ("ADR") program, but even in those instances, no civil fine was imposed.

By way of context, the amounts misstated are quite small when compared to the total amount of money raised and spent by ARMPAC. In 2001, its misstated receipts

³ Misstatement-type issues have also arisen in enforcement matters, but all such matters located by ARMPAC on the public record involved substantial aggravating factors not present in the ARMPAC audit. See MUR 5428 (Republican Party of Arkansas) (numerous issues and no response to interim audit report), MUR 5359 (Paul Williams for Congress) (numerous issues); and MUR 5447 (Missouri Republican State Committee – Federal) (allocation and misstatement issues, overstated cash-on-hand by \$440,480).

constituted a mere 3% of its total receipts, and its misstated disbursements were less than one percent (about 0.5%) of its total disbursements. The same was true of 2002. There, its misstated receipts were 6% of its total receipts, and its misstated disbursements were a mere 2% of its total disbursements. All told for the 2002 election cycle, ARMPAC raised \$3,631,280 and expended \$3,709,757. The auditors took issue with a mere 3% of these totals.

The public record indicates that the Commission typically takes no further action in such matters, or otherwise resolves such findings through ADR. For example, the Commission resolved ADR 167 (signed October 24, 2004) without the imposition of a civil penalty. In that matter, the Tim Johnson for South Dakota Senate campaign's audit found misstatements in the same range as those found in the ARMPAC audit. Specifically, the Johnson campaign misstated its receipts by 0.6%, and misstated its disbursements by 3%. *See also* ADR 163 (Sullivan for Congress) (no penalty imposed, despite a failure to file debt).

By way of comparison, matters in which a fine was imposed had either aggravating factors, or the amount of misstated activity was a much higher percentage of the total raised and spent (such matters were still resolved through ADR, not enforcement). For example, in ADR 144 (Women's Campaign Fund, signed May 19, 2004), the audit that revealed the PAC misstated its receipts by almost 20% and its disbursements by almost 20%. Even with these high percentages, the PAC paid a small \$750 fine.

In ADR 178 (Lindsey Graham for Senate, signed October 18, 2004), the campaign paid a \$10,000 penalty. Unlike ARMPAC's small percentages at issue, the

Graham campaign misstated its 2002 receipts by 77%. Significantly, the Graham audit found the final cash-on-hand for the cycle off by \$83,820 – significantly greater than ARMPAC’s \$27,020 for the cycle (a cycle in which ARMPAC raised and spent over \$7 million, a figure that dwarfs the activity of the Graham campaign).

In sum, in audit-driven matters presenting similar facts to those found in the ARMPAC audit, the audit findings have not warranted further Commission action, or have otherwise been addressed through ADR. Civil penalties have been in scale with the magnitude of the amounts at issue, and in matters like the present ARMPAC matter, no civil penalty was imposed. Thus, the Commission should not take further action.

B. Reporting of Debts and Obligations

The Audit Division (and in turn, the complainant) concluded that ARMPAC failed to report “debts owed to 25 vendors” totaling \$322,306. Final Audit Report at 7. Following the auditors’ recommendation, and although it disagreed with the auditors’ interpretation of Commission regulations, ARMPAC amended its reports and listed the amounts as debt.

Regardless of whether or not the Commission agrees with ARMPAC’s reading of the regulations or opts for the more expansive reading employed by the Audit Division, the result is the same: further Commission action is unwarranted, and any such action would be inconsistent with past Commission practice.

The Commission has consistently resolved such vendor “debt” issues that arise in the context of an audit by requiring that respondents “correct” the public record. Once that is accomplished, the Commission’s own past actions suggest that respondents do not face additional penalties. In fact, there are a number of audits where this type of

reporting issue arose, subsequently cured by way of amendment, and no referral of the finding seems to have been made at all, either to enforcement or alternative dispute resolution. *See* Missouri Democratic State Committee Audit (alleged debts of \$620,575); Republican Party of Arkansas Audit (alleged debts of \$25,332); North Dakota Democratic-Nonpartisan League Party Audit (alleged debts of \$104,788); DRIVE Audit (alleged debts of \$224,303); Women's Campaign Fund Audit (alleged debts "as much as" \$82,777); and Democratic State Central Committee of Maryland Audit (alleged debts of \$95,544).

Even in matters where debt reporting was a significant issue that was resolved through ADR, civil fines were not imposed. For example, in ADR 162, the Braun for President committee failed to report a disputed debt owed to a vendor (who was also the complainant). The remedy was an agreement to amend its reports. In ADR 163, the John Sullivan for Congress campaign admitted it failed to report debt due to software problems and a debt dispute with a vendor. It agreed to enhance compliance and send staff to a seminar. In ADR 079, the Bexar County Democratic Party failed to report continuously \$62,193, but similarly agreed to pursue better compliance in the future, and no civil penalty was imposed. In ADR 036, the Van Horne campaign misreported debt, amended its reports, and as was the case in the other matters, promised to do better.

Moreover, the Audit Division's reading of Commission regulations is overly broad, and inconsistent with past Commission practice, which has resulted in an inflated amount of supposed "debt." Although both the Act and Commission regulations specify that certain "debt" needs to be reported, neither define the term "debt." However, the language of the Act suggests that "debt" be given its common meaning, as it speaks in

terms of “outstanding debts.” 2 U.S.C. § 434(b)(8) (requiring that “outstanding debts and obligations owed by or to” a political committee shall be reported)(emphasis added).

Although broader than the statute, Commission regulations acknowledge this as well, as regularly reoccurring administrative expenses are not reportable as debt before the payment due date. 11 C.F.R. § 104.11(b). Similarly, that same section requires the reporting of other “debt” only after the debt is “incurred.” *Id.* Even the Commission’s *Guide for Non-Connected Committees* supports this reading, as it defined “debt” to include “[u]npaid bills.” *Guide* at 45. Ultimately, such language provides a trap for the unwary, as it is far from clear what exactly constitutes reportable “debt” and what does not.

At issue here are not “debts” as either ordinary people or financial professionals understand that term. When one thinks of “debt,” it generally means that money owed is past due, or that one is in arrears in some fashion. For example, Webster defines “debt” to mean “[t]hat which is due from one person to another,” and “the state of owing something to another.” *The New Webster Encyclopedic Dictionary of the English Language* (1980 ed.). Moreover, synonyms of “debt” include “indebtedness,” “arrearage,” and “due.” *Webster’s Collegiate Thesaurus* (1976). Another dictionary defines “debt” as “[s]omething owed, such as money, goods, or services.” *The American Heritage Dictionary of the English Language* (4th ed. 2000).

The Audit Division, however, took a much more expansive view of what constitutes reportable “debt,” declaring that “debt” includes essentially everything under the proverbial sun, regardless of whether it is “outstanding debt” as stated in the Act, or whether it is actually a debt that has been “incurred,” as contemplated by the regulations.

In other words, in the view of the auditors, it was irrelevant when payment was due, whether or not payment was made in a timely manner, or whether or not payment was past due or otherwise outstanding. Equally irrelevant to the Audit Division was when the so-called "debt" was actually incurred, or whether it was even incurred at all.⁴

To use accounting terms, the Audit Division wishes impose an accrual-based accounting methodology onto what is a cash-based operation.⁵ Campaigns and political committees are premised upon a cash-based accounting system -- money is reported when it actually comes in the proverbial door and is deposited, not when a contributor pledges to make a contribution, or the like. Simply having promises of future contributions does not create any sort of accounts receivable, value or equity. Instead, political committees (and most political consultants and fundraisers) use the cash-accounting method -- which makes sense, as it gives the most accurate picture of what one actually has, a critical determination in the unpredictable world of politics.

But despite this cash-based premise and culture, the auditors have grafted an accrual-based system onto political committees like ARMPAC. Such a hodge-podge of mismatched accounting methods (which as a practical matter cannot be used simultaneously) is bound to cause confusion and "reporting errors."

Compare the auditors' expansive, all-encompassing view of what constitutes reportable "debt" with the more realistic approach utilized by the Commission in MUR

⁴ Obviously, if a vendor failed to perform a service, a political committee cannot possibly be considered to have incurred any sort of debt or obligation to that vendor. But the Audit Division's approach ignores such realities, and treats everything as reportable "debt," whether incurred or not. The Commission has, however, rejected this mentality in the past. See LA Host Committee Audit Report at 5 (the Commission, rejecting Audit's recommendations, concluded (sensibly) that unused letters of credit were not a "debt or obligation").

⁵ In an accrual-based system, sales are recorded when the sale occurs, no matter when payment is actually made. Expenses are incurred when goods or services are received, even though the bill may not be paid until a later date. In a cash-based system, sales are recorded when payment is received, and expenses are incurred when the bills are paid.

4742. In that MUR, a campaign contracted with a political consultant, paid the consultant monthly pursuant to the contract, but also deferred some of its payment until over six months after the election. Neither the monthly payments, nor the deferred compensation scheme were reported as debt. Significantly, the respondent was not penalized for a failure to report its monthly payments due under the contract as "debt." The respondent did pay a small penalty, however, for not reporting the deferred compensation scheme as debt, as that was in fact money owed to the consultant.

MUR 4742 illustrates a critical distinction that is lost in the auditors' analysis. This is not a situation where a respondent did not pay within a commercially reasonable time, attempted to defer payment, or otherwise not pay for a service rendered, or where a respondent did not report such legitimate debt. On the contrary, the Audit Division did not dispute that all vendors were paid by ARMPAC in a commercially reasonable time and in accordance with the various commercial agreements it had with its vendors.⁶ Nor is there any dispute that such expenditures were fully reported on ARMPAC's reports filed with the Commission.

Thus, the Commission should be consistent with its past practice, accept ARMPAC's good-faith amendments and full cooperation with the audit division, and decline to take further action with respect to Finding 2 (or any similar accusation set forth in the complaint).

C. *Non-federal Funding of Federal Activity*

The auditor's final finding concerned one of the most technical aspects of Commission regulations: administrative and fundraising ratios. Although ARMPAC did

⁶ Thus, CREW's speculation on this point is without merit.

not agree with the auditors' findings in some instances, it nonetheless cooperated fully and made all recommended amendments.

26044142670

Recently, the Commission resolved a similar (albeit more complicated) matter through its ADR program. In ADR 204, the Commission resolved a matter against Volunteer PAC that included, among other things, its improper ratio used for the payment of generic get-out-the-vote activities ("GOTV"). Volunteer PAC mistakenly used the ratio applicable to the Republican Party of Tennessee. This mistake caused Volunteer PAC's non-federal account to pay more than its share of the allocable GOTV expenses. In addition to this problem, the auditors also found a myriad of other problems, including misstatement of financial activity, a failure to report \$183,000 in earmarked contributions, and a failure to adequately disclose \$281,000 in disbursements. The matter was resolved through ADR, with the respondent amending its reports and paying a \$10,000 fine for all its violations. This shows, even with all the violations in the matter, the Commission has not treated this particular issue harshly.

Obviously, Volunteer PAC made numerous mistakes, none of which are present here, with the exception to the overhead ratio, where ARMPAC made a similar misstep. In paying for its administrative and generic GOTV expenses, ARMPAC calculated its ratio based upon both direct and indirect candidate support. Based upon this calculation, it arrived at a ratio of 50% federal to 50% non-federal. Unfortunately, the ratio of direct candidate support was 93% federal and 7% non-federal, as ARMPAC did not spend enough non-federal money in direct contributions to non-federal candidates.

By way of context, the change in the ratio constituted less than 0.2 % of the total federal money raised and spent by ARMPAC. In terms of actual dollars, the amount is

less than the amount at issue in the Volunteer PAC matter (\$121,456 vs. \$166,067). Moreover, ARMPAC has already filed corrective amendments, treating the overpayment in a manner similar to how Volunteer PAC resolved the matter. *See* ADR 204 Negotiated Settlement at ¶ 8 (“In addition, Respondents provided evidence of the reimbursement . . . to the non-federal account, filed amended disclosure reports to reflect that reimbursement, and then distributed those funds to non-federal entities.”).

The remaining findings in the ARMPAC audit also concerned ratios, but focused on fundraising expenses. First, the auditors took issue with ratios used in conjunction with eight so-called “donor fulfillment” events – meaning, donors of a certain financial level were invited to attend these events. ARMPAC established the ratios for these events based upon its own good-faith calculations, and the auditors tweaked the ratios slightly. For example, for one event, ARMPAC used a 20/80 ratio, whereas the auditors believed the proper ratio was 17/83. For another event, ARMPAC used a 15/85 ratio, whereas the auditors would have used a 12/88 ratio. Such detailed tinkering did not affect overall totals in a significant way – ultimately, ARMPAC’s non-federal account overspent a mere \$8,205, a miniscule amount when compared with ARMPAC’s overall fundraising.

Second, the auditors took issue with how ARMPAC paid several of its fundraising consultants. Although ARMPAC disagreed with the Audit Division’s legal analysis, it nonetheless cooperated fully with the auditors, and filed all recommended amendments. ARMPAC had entered into two written contracts per each fundraising consultant – one covered federal fundraising, the other covered non-federal fundraising. ARMPAC then paid its fundraising consultants pursuant to these written contracts

26044142672

directly from its federal and non-federal accounts, respectively. In the course of the audit, ARMPAC was asked to and did provide signed and executed affidavits from its fundraisers confirming that the consultants adhered to their respective contracts, and only were paid out of the non-federal account for non-federal fundraising, and were only paid out of the federal account for federal fundraising.

Despite these written contracts and subsequent affidavits (requested by the auditors), the auditors nonetheless concluded that “[d]ocumentation provided to date does not show a separate non-federal fundraising activity.” Final Audit Report at 10. In light of what it called “the absence of documentation,” the Audit Division simply took an average of the 8 fundraising events, and unilaterally decided that the average ratio would serve as the “correct” ratio for the fundraising consultants. Although ARMPAC disagreed with the auditors’ methodology, it nonetheless wished to remain fully cooperative and follow all recommendations of the auditors. Accordingly, it amended its reports to reflect the “correct” ratio, and its repayment from the federal account.

Ultimately, the amount at issue with respect to administrative and fundraising issues is not even 3% of ARMPAC’s total federal fundraising and spending. Because of this small amount at issue, and in light of the Commission’s resolution of a similar manner through ADR, albeit one that involved more violations and higher total amounts at issue, the Commission ought not pursue enforcement action here.

IV. CONCLUSION

Despite a full audit, the Audit Division did not uncover any substantive violations of the Act or Commission regulations. Instead, the auditors only raised various reporting issues of the sort that have not been subject to Commission enforcement action. Those

reporting issues have already been corrected by ARMPAC; thus, based upon past Commission action (or more particularly, inaction), further Commission action is not warranted here.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'D. McGahn II', with a stylized flourish at the end.

Donald F. McGahn II
McGahn & Associates, PLLC
601 Pennsylvania Ave., NW
Suite 900, South Building
Washington, DC 20004
(202) 744-3997

Counsel for Americans for a Republican Majority

26044142673